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TAGS: [EFIN](#) [EREL](#) [ETRD](#) [PGOV](#) [PREL](#) [XH](#) [UP](#)
SUBJECT: UKRAINE: PROMINVESTBANK FAILURE TEST CASE FOR NBU

REF: A. KYIV 2142
[1](#)B. KYIV 2105

Classified By: Edward Kaska for reasons 1.4 (b) and (d)

[1](#)1. (C) Summary and comment: Liquidity problems, a run on deposits, and a possible corporate hijacking at Prominvestbank, Ukraine's sixth largest bank, last month contributed to the run on other Ukrainian banks, which were already jittery due to the world financial crisis (refs). The Acting Chairman of the Security Service of Ukraine has blamed an unnamed criminal organization based in Donetsk oblast for the corporate hijacking. Nationalizing Prominvestbank appears unlikely, given that the anti-crisis legislation recently approved by the Rada (parliament) and signed by the President does not provide the necessary funding. Ukrainian Finance Minister Viktor Pynzenyk on November 5 told U.S. Treasury officials that a decision had been made to sell Prominvestbank to an unnamed strategic investor. Rumors abound as to the identity of the buyer, with many media outlets claiming the Party of Regions deputies and siblings Andrei and Sergei Kluyev are behind the deal.

[1](#)2. (C) The NBU has a choice with Prominvestbank: it can try to sell it to a strong, financially sound bank with the management know-how needed to turn the institution around. Alternatively, it can give it to other business interests with little or no experience in modern banking, but which have the wherewithal to pay or otherwise secure themselves a sweetheart deal. The NBU's decision will shed light on whether it wants to use Prominvestbank as a showcase example of how best to deal with troubled banks in Ukraine. End summary.

Corporate Hijacking at Prominvestbank?

[1](#)3. (U) Volodymyr Matviyenko, Prominvestbank's main shareholder, publicly said in September that the bank had been subject to a "raider attack," or corporate hijacking, aimed at lowering Prominvestbank's capitalization before takeover talks. Matviyenko and his family members who own an unknown percentage of Prominvestbank's equity, have attempted to find a buyer for more than two months (Note: Before he founded Prominvestbank in 1992, Matviyenko from 1987 to 1991 was the chairman of the board of the Ukrainian SSR's branch of Promstroybank. He also was briefly chairman of the NBU in [1](#)1991. Before the financial crisis, Matviyenko reportedly was worth almost \$1 billion. End note.)

[1](#)4. (C) Corporate hijackings are commonly called "raider attacks" in Ukraine, but their perpetrators have nothing in

common with corporate raiders launching unfriendly takeover attempts in more developed equity markets. Business syndicates in Ukraine usually carry out corporate hijackings by bribing courts and law enforcement officials to wrest control of a company from legitimate owners. They often use obscure regional courts because they are cheaper to bribe and faster than other courts. According to the Ukrainian Entrepreneurs' Anti-Raider Union, about 2,500 corporate hijackings have occurred in Ukraine over the last four and a half years. The GOU recently announced plans to take vigorous action against corporate hijackers, and even resuscitated a long-dormant government/private sector working group tasked to deal with the problem.

SBU Chief Blames Criminal Conspiracy

15. (SBU) The Acting Chairman of the Security Service of Ukraine (SBU), Valentyn Nalyvaychenko, in mid October told reporters that a criminal group in Donetsk was behind Prominvestbank's problems and had attempted to embezzle UAH 400 million (\$80 million). The group reportedly stole the money from funds that Prominvestbank used to pay pensions and salaries in the Donetsk region. According to Nalyvaychenko, the conspirators tried to cover up the embezzlement by undermining the bank's financial stability. In addition, they allegedly called Prominvestbank customers and sent text messages to their mobile phones, encouraging them to withdraw their money from the bank. The group also placed infomercials in newspapers and minibuses that reportedly attempted to blacken Prominvestbank's reputation. All of these activities reportedly were financed with a portion of the money that was embezzled. Nalyvaychenko added that the group used Donetsk-based bank Unikom, which he said is owned by Bloc Yuliya Tymoshenko Rada (parliament) deputy Oleksandr Shepelev. For his part, Shepelev publicly denied the allegations and said he would sue Nalyvaychenko for tarnishing his reputation.

Liquidity Woes Worsened Bank's Position

16. (U) Problems at Prominvestbank, which is heavily invested in the metals sector, worsened following the drastic drop in demand for Ukrainian steel products. The bank could not refinance its debt and in September requested a \$1 billion loan from the National Bank of Ukraine (NBU). The NBU subsequently approved a UAH 5 billion (\$833 million) yearlong credit line at the end of September. However, due to what it perceived as Prominvestbank's poor management of the crisis, the NBU in early October announced that it would manage the bank for up to one year and declared a six-month moratorium on paying Prominvestbank's creditors. Prominvestbank reportedly misrepresented short-term deposits as periodic investment on its books and used those funds to refinance long-term loans. The NBU appointed NBU Deputy Head Volodymyr Krotiyuk as interim manager of Prominvestbank.

17. (C) Widespread media coverage of the run on Prominvestbank, combined with news about the world financial crisis and failures of large western banks, caused a panic among Ukrainian depositors. They began withdrawing their deposits and cash, causing long lines at cash machines across the country. In one week, over \$3 billion worth of deposits, or 4.3 percent of all deposits, were withdrawn from Ukrainian banks. Seeking to calm investors and depositors, President Yushchenko and Prime Minister Tymoshenko in October said that Prominvestbank's problems are due to an isolated corporate hijacking and not the result of the world financial crisis.

Prominvestbank Probably Won't be Nationalized

18. (C) Although some high-level Ukrainian politicians, including Tymoshenko and Rada Speaker Arseniy Yatsenyuk, have called for Prominvestbank to be nationalized, the anti-crisis legislation that the Rada passed on October 31 and President Yushchenko signed on November 3 does not contain any

provisions that would allocate budget funds to either Ukreximbank or Oshchadbank, Ukraine's two largest state-owned banks, to take over Prominvestbank. The first draft of the anti-crisis package earmarked UAH 1 billion (about \$167 billion) for Ukreximbank to buy Prominvestbank, but Ukreximbank representative Viktor Kapustin told reporters that he was against using Ukreximbank to help keep Prominvestbank afloat because it would only hurt Ukreximbank.

Deputy Ukreximbank Chairman Mykola Oudevechenko told us on October 31 that his bank stoutly refused to assume responsibility for Prominvestbank. Ukreximbank's impeccable credit standing would have suffered a steep discount to book value because nobody knew the true extent of Prominvestbank's problems, Oudevechenko told us. Moreover, NBU Governor Volodymyr Stelmakh on October 22 publicly said that the NBU does not intend to expand the loan facility already provided to Prominvestbank and called for a strategic investor to be brought in immediately to help resolve the bank's problems. Finance Minister Viktor Pynzenyk told U.S. Treasury officials that a decision had been taken to sell Prominvestbank, but Pynzenyk refused to name the buyers.

Why Buy Prominvestbank?

¶9. (SBU) Stelmakh in early October said that Prominvestbank has a sound loan portfolio. Before Ukraine's financial crisis, the total volume of Prominvestbank's assets (UAH 27.5 billion, or \$5.7 billion) placed sixth out of 178 Ukrainian banks and represented almost 4 percent of the Ukrainian banking system's assets, according to the NBU. Matviyenko has said he thinks the bank is worth as much as \$4 billion, while experts expect Prominvestbank to sell for \$1.2 billion.

The temporary NBU administration at Prominvestbank has noted that the main shareholders (about eight to ten people) have the option to sell about 80 percent of the bank's shares.

Party of Regions Deputies Get Sweetheart Deal?

¶10. (SBU) Although interest in acquiring Prominvestbank has been robust, few concrete details about potential buyers and the negotiating process are known. So far, a consortium represented by Party of Regions deputies Andrei Kluyev, Sergei Kluyev, and Valentyn Landyk appear to be the leading contenders, according to media reports. Some media reports also claim that former Prime Minister and Party of Regions head Viktor Yanukovich and representatives in the General Procurator's office support the Kluyevs' efforts to purchase Prominvestbank. Press have reported that the Kluyev brothers already acquired a 70 percent stake in Prominvestbank and appointed Igor Frantskevich, former representative of Indeks Bank and Raiffeisen Bank Ukraine, to take over NBU Deputy Head Krotiyuk's interim administration at Prominvestbank. Frantskevich reportedly began work at Prominvestbank on November 4. Moreover, some reports claim that the brothers Kluyev received for free 50 percent of the 70 percent stake they acquired.

¶11. (C) The Kluyevs months ago started taking steps to buy Prominvestbank. They reportedly offered the Matviyenko family \$1 billion for their Prominvestbank shares and then subsequently lowered their offer to \$300 million. Some argue that once financial markets recover the Kluyevs intend to sell Prominvestbank at a steep mark-up, which could help beef up the Party of Regions war chest as it prepares for the presidential election in late 2009.

Kluyevs: A Front for More Well-Heeled Interests?

¶12. (C) Some experts have questioned the Kluyevs' capability to come up with the capital needed to conclude the deal, given the recent liquidity crisis in world financial markets and the Kluyevs' net worth, which amounts to only \$600 million. According to some estimates, to buy Prominvestbank an investor would need to provide \$1 billion to resolve the bank's liquidity problems, pay \$400 million for the bank's

statutory capital, and return \$1 billion to the NBU for loans Prominvestbank received. The media has no shortage of theories about who might be behind the Kluyevs.

Other Big Players Also Jockey for Prominvestbank

¶13. (SBU) Another consortium consisting of Russia's Alfa Bank and Mykola Lagun, co-owner of Delta Bank and representative of a group of investors, also sought to acquire Prominvestbank. According to media reporting, the consortium of investors Lagun represented reportedly included Ukrainian oligarchs Viktor Pinchuk, Dmitriy Firtash, and Russian metals magnate Alisher Usmanov. Separately, Russian bank Sberbank in October appeared poised to conclude a deal, but no longer seems to be in the running.

¶14. (U) No matter who concludes a deal with Prominvestbank's current shareholders, it must be approved by the NBU, according to NBU Governor Stelmakh. The director of the NBU's legal department, Vassiliy Pasechnik, would be responsible for providing approval, but he reportedly is on vacation. It is unclear whether his deputy, Vladimir Novikov, is authorized to approve any deal to purchase Prominvestbank.

¶15. (SBU) Comment. The deal to acquire Prominvestbank from the Matviyenko family has been nontransparent and fraught with shenanigans from the start. Given the fluidity and opaqueness of the situation, a different consortium could still emerge as the majority shareholder of Prominvestbank, despite the flood of news about the Kluyev deal. It also cannot be ruled out that the GOU may step in at the eleventh hour to halt the deal with the Kluyevs. While a private bank probably has the resources to better manage Prominvestbank than the state, it's unclear whether selling the shares instead of nationalizing them will reassure Ukrainian depositors and restore confidence in the Ukrainian banking system. The NBU's actions on Prominvestbank will shed light on whether it wants to use Prominvestbank as a showcase example of how best to deal with troubled banks in Ukraine. End comment.
TAYLOR